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Upping the Ante for Whistleblowers: New Regulatory Reform Act Incentivizes Whistleblowers to Disclose Potential Violations of the Foreign Corrupt Practices Act to the Government

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Among its sweeping regulatory reforms aimed at the financial industry, a little-noticed provision of the Restoring American Financial Stability Act of 2010 (the "Act") likely will have a substantial impact on public companies subject to the U.S. Foreign Corrupt Practices Act (FCPA) by incentivizing "whistleblowers" who provide original information to the Securities and Exchange Commission (SEC) with a bounty in the event the SEC later recovers damages or penalties from the companies. While the potential bounty is not limited to FCPA cases, this whistleblower provision will open up yet additional avenues for the SEC and Department of Justice (DOJ) to investigate and prosecute FCPA violations.[1] If enacted, the new legislation may lead to an increase in SEC-initiated actions that would reach a host of public companies operating in many industries. Although not yet signed into law, congressional leaders have resolved the differences between the House and Senate bills, and aim to pass a final bill to be signed by the President before July 4. So that companies may understand the potential impact of the new Act, we provide below a brief summary and a comparison of the whistleblower provision to a similar provision in the False Claims Act (FCA).

Since the Civil War, the FCA has contained a provision that empowers private plaintiffs to bring *qui tam* lawsuits against individuals and companies suspected of defrauding the government, both for themselves and on behalf of the United States. In such actions, the government may choose to intervene in the case, or to allow the private plaintiff (known as a "relator") to proceed alone. Depending on a number of factors, including the importance of the relator's efforts to the success of the case, the relator may receive a percentage of the government's recovery. Because recoveries under the FCA can be substantial (usually three times the actual damages, plus the relator's expenses, plus a penalty of $5,500 to $11,000 per violation), the relator's award is a substantial inducement to come forward with information regarding potential fraudulent activity.

The new Act shares a number of features with the FCA whistleblower provision, but as explained below has a narrower reach than the FCA, and vests significant discretion in the SEC rather than the courts in whether, and to what extent, a whistleblower should share in the government's recovery. The Act requires the SEC to provide a reward to anyone who provides "original information" leading to the successful enforcement of the securities laws

[1] Restoring American Financial Stability Act of 2010, H.R. 4173, § 922 *et seq.* (2010) (as passed by Senate, May 20, 2010).

in a “covered judicial or administrative action” or a “related action.” Whistleblowers will receive between 10 and 30 percent of the government’s recovery, with the precise award to be determined by the SEC. Whistleblowers will be compensated out of a new Investor Protection Fund, established out of the proceeds of actions resolved based on whistleblower-provided information. In addition, just as in the FCA, whistleblowers may sue their employers if they are discriminated against on the basis of their lawful efforts to stop or report illegal activity. The statute requires the SEC to issue final implementing regulations within 270 days of enactment.

Whistleblowers may recover for past violations.

A whistleblower providing information will be entitled to recover regardless of when the illegal conduct about which he or she reports occurred. For example, a whistleblower may recover an award based on information he or she provides in 2011, leading to a successful enforcement action for a violation of the securities laws that occurred in 2008.

Whistleblowers cannot independently bring actions.

Under the new statute, the whistleblower recovers only if the government prevails on the basis of his or her information. The whistleblower cannot independently bring an action against an alleged violator of the securities laws, and may not proceed alone if the government declines to prosecute the case.

Awards limited to “covered judicial proceedings.”

Unlike the FCA, which allows actions to be brought for any false or fraudulent claim submitted to the government, whistleblowers may only recover if the government prevails in a “covered judicial proceeding,” defined as any judicial or administrative action brought by the SEC resulting in monetary sanctions of over $1 million. Following such a proceeding, the whistleblower may recover a percentage of the total monetary sanctions imposed in the covered proceeding. The whistleblower may also recover in any “related action” brought by another agency, such as the DOJ, which is based on the whistleblower-provided information. This is significant in the FCPA context, as the SEC and DOJ have parallel enforcement responsibility for the FCPA and often cooperate to collectively investigate, but individually penalize, FCPA violators.

SEC has significant discretion in granting awards.

Under the FCA, while the bounds of the relator’s award are defined by statute, courts have some discretion as to the precise amount. The new provision also defines the maximum and minimum award, but the SEC has discretion as to the ultimate amount. In setting the amount of any whistleblower recovery, the SEC will consider the importance of the whistleblower’s information, the degree of assistance the whistleblower or his counsel provided, and the SEC’s “programmatic interest” in deterring violations, as well as additional factors to be included in implementing regulations. Unlike the FCA, the provision makes no

explicit mention of awards upon the government's successful settlement of a case, but does reference paying awards based on successful enforcement, which may include settlements. In addition, the new Act excludes broad classes of individuals from recovery on the basis of their criminal activity, government employment, or duties to disclose under federal securities laws.

Different "originality" requirements.

Under both the new Act and the FCA, rewards are usually not available if the information provided is already publicly available, but the specific requirements of the two statutes differ. The FCA prevents courts from hearing cases based on information disclosed in public proceedings or in the media, unless the relator is the "original source" of the information. The relator is the "original source" only if, prior to a public disclosure, he or she voluntarily disclosed the information, or had knowledge independent of the publicly disclosed information that materially added to the public allegations *and* voluntarily provided this information to the government before filing a lawsuit. By contrast, the new provision allows for rewards if the government prevails on the basis of the whistleblower's "original information." This is defined as information that is derived from his or her independent knowledge or analysis and not known to the SEC from any other source (unless the whistleblower is the original source), and is not derived exclusively from an allegation made in a government proceeding or in the news media, unless the whistleblower is a source of the information. Unlike the FCA, the statute does not define original source.

Representation by counsel.

The new Act allows whistleblowers to be represented by counsel, and in particular, to recover on the basis of anonymous claims made through their attorneys, so long as the attorney discloses the whistleblower's identity before the award is paid.

Confidentiality of whistleblower-provided information.

The new provision empowers the government to keep whistleblower-provided information confidential. Information provided by whistleblowers is exempt from Freedom of Information Act requests, civil discovery requests, and other legal process, and is considered privileged and confidential; however, it can be disclosed to other governmental bodies when "necessary to protect investors."

Judicial review of whistleblower awards.

Whistleblower awards made under the new statute may be appealed to a federal circuit court, and are reviewed in the same manner as other agency actions.

The potential effects of the legislation, particularly in FCPA enforcement, are significant. Over the past decade, the SEC and the DOJ have made prosecution of FCPA violations a top priority. The level of FCPA enforcement and settlements has reached an all time high,

with recent settlement amounts upwards of $500 million. The new Act's whistleblower provision is likely to spark an even greater number of investigations by incenting individuals employed by companies subject to the FCPA to report potential violations directly to the SEC. In addition to the increased risk for scrutiny and investigation, companies subject to the FCPA could find that by incenting direct disclosure by individuals, the Act's whistleblower provision undermines their ability to conduct an internal review and evaluation of any potential violation before disclosing the issue to the government.

For more information, please contact Vinson & Elkins lawyers Craig Margolis, Bill Lawler, Rita Glavin, Yousri Omar, or Carl Jordan. Visit our website to learn more about V&E's Government Investigations and White Collar Criminal Defense or Labor and Employment practices.

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